OZARK FUELS CORP.
FIDELITY AND DEPOSIT COMPANY OF MARYLAND

IBLA 94-496 Decided August 20, 1997

Appeal from decisions of the New Mexico State Office, Bureau of Land Management, holding sublessee and surety liable for lease rental. OKBLM 018074, OKNM 034521.

Affirmed in part and reversed in part.

1. Coal Leases and Permits: Assignments or Transfers

> Upon approval of a sublease of a coal lease based in part on provision by the sublessee of an acceptable lease bond, the sublessee and the surety are generally responsible for all lease obligations. With respect to lease rental for which liability accrues in the absence of relinquishment of the lease, however, it must be recognized that the sublessee has no authority to relinquish the underlying lease. Hence, when a sublessee has notified BLM that an approved sublease has been terminated, a decision holding the sublessee liable for subsequently accruing lease rental will be reversed.

APPEARANCES: Carla W. Hearnsberger, El Dorado, Arkansas, for Ozark Fuels Corporation; Stephanie A. Cole, Esq., Overland Park, Kansas, for Fidelity and Deposit Company of Maryland.

OPINION BY ADMINISTRATIVE JUDGE GRANT

This case involves consolidated appeals by Ozark Fuels Corporation (Ozark), as lessee, and Fidelity and Deposit Company of Maryland (Fidelity), as surety, from separate decisions of the New Mexico State Office, Bureau of Land Management (BLM). The decisions below required payment of past due rental obligations on Federal coal leases OKBLM 018074 and OKNM 034521.

Ozark filed an appeal of a March 21, 1994, BLM determination addressed to Ozark and to Fidelity (as surety) requiring payment of rental for lease OKBLM 018074 in the amount of $978 which had been due October 1, 1992. Ozark appealed the determination on the ground that it had begun the process for dissolution of the corporation in April 1991, and its lease interest reverted to Howe Coal Company (Howe) from which Ozark had obtained its

interest by sublease. This Decision was also objected to by the surety on the lease bond, Fidelity, on the same grounds in a letter dated March 30, 1994. Fidelity requested more information regarding the basis of the asserted liability. In a followup letter dated April 6, 1994, BLM indicated that the surety bonds for both OKBLM 018074 and OKNM 034521 (as well as certain other Ozark leases) were provided by Ozark in order to obtain approval of the sublease of the coal leases. In response to this letter, Fidelity disputed its liability in a letter to BLM dated April 12, 1994. Contesting its liability on several grounds, Fidelity asserted that the bond terminated when the lease was readjusted in 1989, that it had written its bonds on behalf of Ozark and had no liability on behalf of Howe, and that Howe became the responsible lessee after the dissolution of Ozark in 1991.

Ozark has also appealed from an April 7, 1994, BLM determination addressed to Ozark as bonded principal and Fidelity as surety. That determination held Ozark to be in default for unpaid rental in the amount of $15,264 1/ on lease OKNM 034521. It also indicated that failure to pay within 60 days would result in referral of the case to the Solicitor to pursue judicial remedies including cancellation of all leases covered by the bond. In appealing, Ozark again asserts that it started the process of dissolution in April 1991, and the leases reverted to Howe.

By Decision dated February 8, 1994, BLM had previously demanded payment by Fidelity under the surety bond for the unpaid rental on lease OKNM 034521. In a letter dated February 15, 1994, Fidelity contested its liability for the rental on the same grounds noted above for lease OKBLM 018074. The BLM responded with a copy of the same letter of April 6, 1994, sent to Fidelity in connection with lease OKBLM 018074. As noted above, Fidelity responded denying liability on the lease bonds as asserted by BLM. 2/

Coal leases OKBLM 018074 and OKNM 034521 have long histories which need not be set forth in detail. Garland Coal and Mining Company (Garland), lessee of both leases, subleased both leases to Howe, by instrument dated April 22, 1967. 3/ The sublease was approved by Decision of BLM

1/ It appears from the record that this figure consisted of lease rental due and unpaid on Mar. 1, 1991 ($7,632), and Mar. 1, 1992 ($7,632).
2/ Although the BLM transmittal memorandum forwarding the case files for OKBLM 018074 and OKNM 034521 recognized the appeals filed by Ozark, no mention was made of an appeal by Fidelity of the BLM Decisions to the extent that they asserted the liability of the surety on the lease bonds. However, it is clear from the record that Fidelity is also appealing liability on the lease bonds. Hence, Fidelity is properly regarded as an Appellant in this case.
3/ Garland later assigned its record title interest in the leases to Howe by assignments approved effective July 1, 1983.

dated January 2, 1968. Subsequently, further subleases of the lessee's interest from Howe to Ozark were submitted for approval. 4/ By Decision dated April 3, 1981, BLM approved the subleases from Howe to Ozark while accepting lease bonds provided by Fidelity as surety for Ozark and terminating the period of liability for Howe's bonds for the leases.

On April 9, 1990, BLM received from Ozark an application for approval of a logical mining unit (LMU) embracing the two coal leases along with other leases. Subsequently, by memorandum dated June 27, 1991, addressing OKNM 034521 and one other lease, the BLM District Manager advised that "[b]ased on the dissolution of Ozark Fuels Corporation and our inability to contact Howe Coal Company concerning formation of a logical mining unit, our recommendation is to terminate the leases for failure to meet the requirement of Section 7 of the Mineral Leasing Act." 5/ Subsequently, BLM was advised by letter of September 24, 1991, from Ozark (received on September 27, 1991) that the LMU application was withdrawn citing the dissolution of Ozark and indicating that its interest in the leases had reverted to Howe. 6/

By separate notices, both dated March 16, 1992, Fidelity notified BLM that it was cancelling bond number 9406114 for lease OKBLM 018074 and bond number 9406118 for lease OKNM 034521 effective 60 days from the date of the notices. In a letter dated May 11, 1992, BLM replied that it could not release liability for the bond on OKBLM 018074 until receipt of a replacement bond or release liability on the bond for OKNM 034521 until it received favorable reports from the Tulsa District Office and the Minerals Management Service (MMS). 7/ By letter dated October 6, 1992, BLM informed

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4/ As part of the subleases, Ozark, as sublessee, agreed to "duly and punctually keep and perform all covenants, agreements, duties and conditions to be kept, performed or met by the lessee, the Original Sublessor and the Sublessor under the terms and provisions of the Leases." (Sublease Agreement at ¶ 4(b).)

5/ 30 U.S.C. § 207 (1994). Section 7 provides in part that "[a]ny lease which is not producing in commercial quantities at the end of ten years shall be terminated." 30 U.S.C. § 207(a); see 43 C.F.R. § 3452.3(a).

6/ Enclosed with the letter of Sept. 24, 1991, was a copy of a letter dated Apr. 23, 1991, addressed to BLM which announced the dissolution of Ozark. The first evidence in the record before us of receipt by BLM of this earlier letter is the date stamp of Sept. 27, 1991, when it was received as an enclosure with the later letter.

7/ The reason for the disparate treatment was that lease OKNM 034521 had terminated effective May 1, 1992, for failure to meet the diligent development requirements pursuant to 43 C.F.R. § 3452.3(a). As a result of the termination, BLM had to determine if any reclamation needed to be completed and if all rental had been paid. Howe, as holder of record title to the lease, and Fidelity were notified of the termination by BLM Decision dated May 19, 1992.

Howe, Ozark, and Fidelity that rental payment in the amount of $15,624 was delinquent for lease OKNM 034521 and that reclamation of the land in the lease remained to be completed. Ozark responded to BLM that only minor reclamation work remained and provided copies of letters to MMS stating that the leases had reverted to Howe. After additional correspondence with Fidelity in regard to both bonds and leases, BLM issued the Decisions requiring payment, and this appeal followed.

[1] This Board has recognized that the assignee of the record title interest in a coal lease agrees to assume the obligations of the lessee upon acceptance, and thus, the liability of an assignee for lease obligations generally attaches once an assignment is approved. Gifford H. Allen, 131 IBLA 195, 202 (1994); see Alaska Statebank, 111 IBLA 300, 308-10 (1989). Further, the relevant regulation explicitly provides that "[a]fter the effective date of approval, the transferee, including any sublessee, * * * and the transferee's surety shall be responsible for all lease, application or license obligations, notwithstanding any terms of the transfer to the contrary." 43 C.F.R. § 3453.2-4(b) (emphasis added). Thus, the obligation to comply with the lease terms applies to an approved sublessee and its surety. See Valley Camp of Utah, Inc. v. Babbitt, 24 F.3d 1263, 1268-71 (10th Cir. 1994). While the sublessee and its surety are bound by the terms of the lease, we do not construe this to mean that the obligation is interminable or necessarily coextensive with the term of the lease. A lessee may terminate his rental obligation under a lease prospectively by relinquishing the lease. See 43 C.F.R. § 3452.1. However, we know of no authority for the sublessee whose title derives directly from the lessee rather than the Government, to relinquish its interest directly to the Government. Cf. Harry L. Bigbee, 2 IBLA 23, 27 (1971) (relinquishment of oil and gas lease upheld over objection of operator on ground that approval of an assignment of operating rights in a lease did not give rise to a contractual relationship between the Government and the operator and did not constitute an assignment of the lease.)

Pursuant to the terms of the approved sublease to Ozark dated July 7, 1980, the sublease was subject to termination upon notification of the lessee by the sublessee or, alternatively, upon failure of the sublessee to commence full scale mining operations on the subleased lands by a certain date. (Sublease Agreement at ¶ 4(e).) The terms of the sublease were subsequently amended to revise the date and require commencement of mining operations by April 1, 1992. (Amendment of Sublease dated Jan. 17, 1989.) In this context, the September 1991 letter to BLM withdrawing the LMU application and indicating its interest had reverted to lessee Howe, citing the dissolution of Ozark, was sufficient to put BLM on notice that the sublease was terminated. In a case where an approved sublessee has announced to BLM its relinquishment of its interest in the sublease to the lessee, we find it inequitable and improper to continue to hold the sublessee liable for future rental obligations. Accordingly, we find that BLM erred in holding Ozark liable for lease rental accruing after September 1991 including the $978 due October 1, 1992, on OKBLM 018074 and $7,632 due

March 1, 1992, on OKNM 034521. It follows, however, that liability for the rent due March 1, 1991, on the latter lease in the amount of $7,632 was properly assessed. Although the apparent dissolution of the sublessee corporation may affect the relief available against the sublessee, no error has been shown in the BLM Decision finding the sublessee Ozark liable for the lease obligation in the latter amount.

With respect to the liability of the surety for Ozark's obligations, we note that Fidelity's assertion that it has no evidence that it consented to liability as surety for the sublessee when the leases were readjusted is not supported by the record. The case record shows that Fidelity did consent to be bound by the bonds after the leases were readjusted. Lease OKBLM 018074 was readjusted in 1989 and in a rider required by BLM and executed at that time to bond number 9406114, Fidelity agreed to be bound "by all the terms and conditions of the lease as readjusted effective October 1, 1989." When lease OKNM 034521 was readjusted in 1982, BLM required an increase in the bond to $10,000, and on March 23, 1982, Fidelity submitted a rider to bond number 9406118 increasing the bond to $10,000. On September 18, 1991, BLM sent a notice of readjustment of OKNM 034521, effective March 1, 1992, to Ozark as sublessee and Howe as lessee, with a copy to Fidelity. The notice required either a replacement bond or a consent of the surety to the existing bond whereby the surety agreed to remain bound by all terms and conditions of the readjusted lease. A Verification Certificate was submitted to BLM by Fidelity in November 1991. That Certificate stated that Ozark's bond number 9406118 for $10,000 remained in effect, "subject to all its agreements, conditions, and limitations." On November 15, 1991, BLM issued a notice accepting the consent of surety for lease OKNM 034521. The notice stated that the "surety agrees to be bound to all the terms and conditions of readjusted Federal Coal Lease OKNM 034521." A copy of BLM's acceptance was sent to Fidelity. Thus, the case record is clear that Fidelity did consent to the bonds when the leases were readjusted.

We note, however, that Fidelity is the surety for the sublessee, Ozark, on the subleases. Thus, to the extent we have found that BLM erred in holding Ozark liable for certain rental payments, the liability of Fidelity is similarly limited.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 C.F.R. § 4.1, the Decisions appealed from are affirmed in part and reversed in part.

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C. Randall Grant, Jr.
Administrative Judge

I concur:

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James L. Burski
Administrative Judge